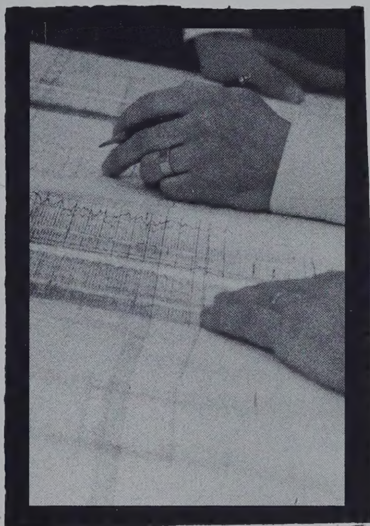

# CALAHOO PETROLEUM

1996
Annual Report

## CORPORATE PROFILE

Calahoo Petroleum Ltd. is a Calgary based, junior oil and gas resource company trading on the Alberta Stock Exchange under the symbol "CLX". The Company has approximately 27 million shares outstanding.

Calahoo was incorporated in 1986. In 1993, a strong new management team was assembled which subsequently directed the Company's business into the exploration, development and production of oil and gas in Western Canada. Calahoo is a rapidly growing, profitable, well-focused public entity.

Over the last three and a half years, the Company's production has grown from 160 barrels daily of oil equivalent to 1,000 barrels daily of oil equivalent, divided between oil (60 percent) and gas (40 percent). Calahoo's strength and focus has been on the acquisition of high quality, long life properties that have the potential for significant production gains. Having built a solid foundation of high netback production and cash flow, Calahoo will step up its exploration activity in the years ahead. Calahoo has made strategic land acquisitions in and around its core areas and has an impressive inventory of economic, low to medium risk drilling prospects. In the coming years, the Company can expect to achieve superior results through the exploration and exploitation of this undeveloped land base and the utilization of its existing infrastructure and its operational experience in these areas. The Company's goal is to increase shareholder value through the cost effective acquisition of, and the exploration and development of high quality oil and gas reserves.

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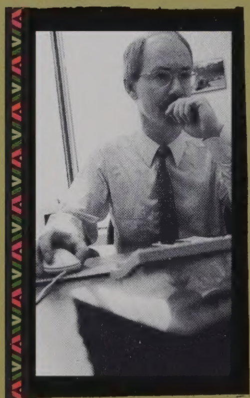


## CORPORATE STRATEGY

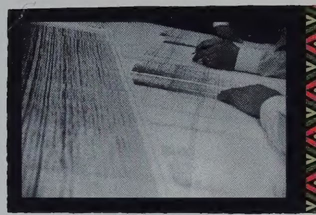
To date, management has focused on acquiring stable long life production that can provide cash flow for further drilling and/or acquisition opportunities. The initial part of the strategy has been achieved and over the next two to three year period, Calahoo will direct a large proportion of its discretionary cash flow into drilling. Currently Calahoo has an excess of quality projects in inventory and will enjoy the success-driven process of bringing only the best prospects forward in the years ahead.

Calahoo will continue to pursue profitable and strategic core area acquisitions. Calahoo plans to acquire a high quality property to develop into another core area for the Company. An important goal for Calahoo is to build a successful, dynamic, intermediate-sized corporation with a relatively small number of major properties.

### ANNUAL MEETING

**The Special and Annual General Meeting for Shareholders will be held at 3:00 p.m. on Tuesday, May 13th, 1997: Cardium Room of The Calgary Petroleum Club, 319 – Fifth Avenue S.W., Calgary, Alberta. All shareholders are encouraged to attend and participate in the business of the meeting. Those unable to do so should complete the form of proxy and forward it at their earliest convenience.**

The Company will be active and desires to operate. Consideration will also be given to joint venture exploration/development opportunities which are operated by efficient, experienced companies with a successful track record. We believe that maintaining high interests in our properties will result in low general and administrative costs relative to production. Corporate debt will be maintained at a manageable level relative to cash flow.



## corporate highlights

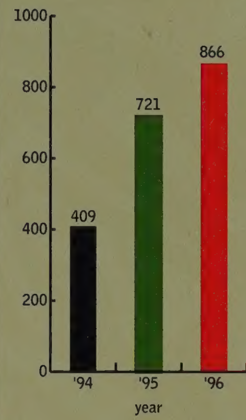
| Financial<br>($ thousands, except per share data) | 1996 | 1995 | % Change |
|---|---|---|---|
| Gross Revenue | **7,001** | 4,906 | 43 |
| Cash Flow from Operations | **3,396** | 2,212 | 54 |
| Per Share ($) | **0.16** | 0.13 | 23 |
| Net Earnings | **652** | 567 | 15 |
| Per Share ($) | **0.03** | 0.03 | — |
| Capital Expenditures | **5,760** | 5,093 | 13 |
| Long-Term Debt | **4,071** | 6,828 | (40) |
| Shareholders' Equity | **12,261** | 7,770 | 58 |
| Common Shares Outstanding at Dec. 31 | | | |
| Basic (thousands) | **26,676** | 18,941 | 41 |
| Fully Diluted (thousands) | **35,018** | 20,395 | 72 |
| Average Weighted Shares Outstanding | | | |
| At December 31 (thousands) | **20,994** | 17,692 | 19 |

### Operations

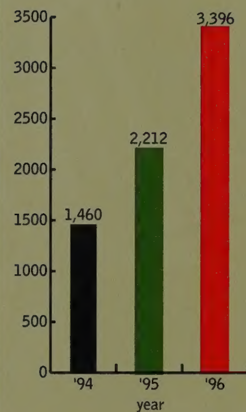
| Production and Prices (average) | | | |
|---|---|---|---|
| Crude Oil and NGL Production (bbls/d) | **551** | 471 | 17 |
| Price ($/bbl) | **27.93** | 22.67 | 23 |
| Natural Gas Production (mcf/d) | **3,153** | 2,498 | 26 |
| Price ($/mcf) | **1.37** | 1.04 | 32 |
| Average Production BOE/d | **866** | 721 | 20 |
| Proven Reserves (mBOE) | **2,525** | 2,060 | 23 |
| Proven and Probable Reserves (mBOE) | **3,670** | 3,110 | 18 |

| Exploration and Development | | | |
|---|---|---|---|
| Wells Drilled | | | |
| Gross | **14** | 7 | 100 |
| Net | **7.1** | 2.3 | 209 |
| Land | | | |
| Net Acres (thousands) | **53,332** | 31,000 | 72 |

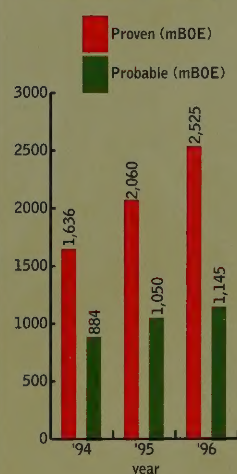
**production**
(BOE/d)

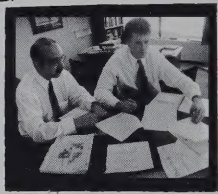


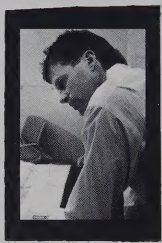

**cash flow from operations**
(in thousands of Canadian $)




**reserves**
(in thousands of Canadian $)







## PRESIDENT'S MESSAGE

Calahoo's management team and Board of Directors are pleased to report another year of growth for the Company. Production as of January 1, 1997 was approximately 1,000 BOE/d, up 15 percent from first quarter production of 873 BOE/d. During 1996, total proved reserves increased by 23% to 2,525 mBOE's.

### Summary

In 1996, our Company met its financial objective of attaining cash flow per share of 16¢. Average daily production during the year was 866 BOE/d, up from 721 BOE/d in 1995. While 1996 production fell short of our target of 1,000 BOE/d, the Company still successfully replaced its production by 2.6 times, added total reserves at a cost of $5.82 per BOE and showed a profit of $0.7 million or 3 cents per share.

In June 1996, Calahoo completed a private placement, raising $1.6 million. In December 1996, Calahoo completed a flow-through/warrant equity financing which raised $2.7 million. Both financings had warrants attached and, if exercised, will provide Calahoo with $4.6 million in 1997. This capital will be put towards Calahoo's exploration and development activity.

For the upcoming year, Calahoo anticipates an acceleration in growth fueled by a $14 million capital program. The funds will allow the Company to drill a record number of wells and to purchase more production and prospective land. Approximately half of the 1997 budget will be allocated to a high graded drilling program. The continued evaluation and purchase of partners interest and offsetting producing or prospective properties within Calahoo's core areas will continue to be an important objective for management. Calahoo also intends to establish another core property in Alberta through an acquisition and follow-up development activity.

The industry itself has more capital to spend in 1997, which will increase competition among companies. Calahoo is keenly aware of this and therefore will be focusing its efforts in 1997 on exploration and development plays generated in-house. Rig availability is a concern for Calahoo. The utilization of rigs is at a peak and to date, the Company does not have a rig contracted. Management has placed a high priority on securing rigs, and expects to have rigs available to drill on "windows" for the period of June through to December.

Oil and gas prices experienced during 1996 were extremely strong and made a significant contribution to the bottom line. Calahoo anticipates another good year for oil and gas pricing in 1997 and has forecast its yearly average oil prices based on $20 US/bbl WTI and a corporate average of $1.35/mcf for gas. Calahoo has hedged 250 bbls/d of oil production at $23 US/bbl for the second quarter of 1997.

Our corporate strategy of increasing shareholder value through cost effective acquisition, exploration and development of high quality, long life oil and gas reserves will continue to provide Calahoo with the potential for consistent, profitable growth.

### Nineteen Ninety-Six Results

As a result of higher production and higher commodity prices, Calahoo achieved its targets for cash flow. Cash flow for the year was $3.4 million up from $2.2 million in 1995. Cash flow per share increased 23 percent to 16 cents per share in 1996, compared to 13 cents per share in 1995. Net earnings increased by 15 percent to $0.7 million. Calahoo's long-term debt decreased by 40 percent to $4.1 million as of December 31, 1996. Forecasted cash flow for 1997 is $5.8 million.

Operationally, Calahoo successfully added to its long life, high quality reserves in 1996, replacing production by a factor of 2.6. As of January 1, 1997 the Corporation's discounted (15 percent) total proved plus risked probable reserve value is $23.6 million (3,098 mBOE's). Based on the reserves and 1996 annual production, Calahoo has a reserve life of 9.8 years. Overall yearly production from all sources net of declines and property dispositions increased by 120 BOE/d. Calahoo also increased its undeveloped land holdings. The undeveloped land provides the Company with numerous exploration and development opportunities.

In 1996, Calahoo's capital expenditures totalled $5.8 million, of which $1.3 million was spent on property acquisitions and $3.6 million on drilling, completions and production optimization. The balance of $0.9 million was invested into land purchases and seismic programs. New production resulting from Calahoo's 1996 capital program totaled 250 BOE/d. Calahoo expects further cost-effective production gains on its core properties in the years ahead.

Incremental proven reserves assigned to Calahoo's 1996 acquisitions and drilling program is 815 mBOE. Proven finding and development costs for the year averaged $7.07/BOE, inclusive of all expended capital. (See Operations Review.) Excluding land and seismic, Calahoo's proven finding and development costs were $6.01/BOE. Given the quality and life of the reserves, this is a competitive number for a junior oil and gas company. In 1996, operating field netbacks on Calahoo's light oil and sweet gas production averaged $14.50/BOE and corporate netbacks (net of G&A and interest) were $10.72/BOE.

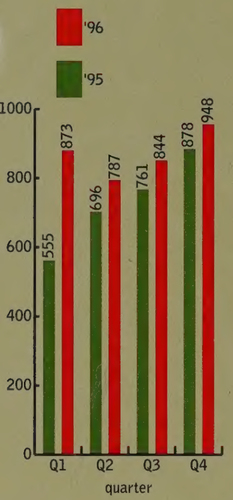
### Acquisition/Property Swaps

In 1996, Calahoo completed a number of property acquisitions in and around in its core areas for a total of $1.3 million. Overall, the majority of Calahoo's purchases were directed towards gas properties as management believes that gas prices will improve in the years ahead.

At Stoddart, an important core property in British Columbia, Calahoo acquired the interests of two joint venture partners in a light oil pool. These acquisitions, which occurred in the first quarter of 1996, increased Calahoo's working interest to 90 percent in two producing oil wells and in one and a half sections of undeveloped land. Calahoo also recently acquired a 67% interest in a Stoddart gas well and in two sections of undeveloped land offsetting Company lands. The effective date of this latter purchase was November 1, 1996.

In two separate acquisitions on properties in the Buick Creek area to the north of Stoddart,

average quarterly production
(BOE/d)




Calahoo acquired a 100% working interest in three suspended gas wells and a 19% non-operated interest in two capped gas wells. The Company is planning on restoring production from the suspended wells in 1997. Immediately south of Fort St. John, Calahoo upgraded its working interest in a capped gas well from 31% to 53%. It is anticipated that the capped gas wells will be placed on-stream in late 1997 or early 1998.

Total 1996 capital allocated to acquisitions was $1.3 million. Production of 71 BOE/d was purchased along with capped deliverability of 200 BOE/d. Proved reserves acquired amounted to approximately 270 mBOE's. Included in the acquisitions was 2.5 net sections of undeveloped land.

### Drilling–Operated

The total net cost of Calahoo's 1996 operated drilling program was approximately $2.7 million and included eight wells. Two development wells and one exploratory well were drilled for oil in British Columbia. A development well in the Fort St. John area and a Siphon area exploratory well were dry and abandoned. A Stoddart area development well is currently producing 63 bbls/d of light oil. The success of the Stoddart well justifies follow-up drilling which will be pursued in 1997. In the Sedalia/Oyen area of eastern Alberta, Calahoo drilled five wells for gas. Three wells were successfully cased and completed for gas production and two wells were dry and abandoned. One well was brought on-stream in September and is currently producing 0.6 mmcf/d net to the Company. The other two wells were brought on-stream in March 1997 at a combined net rate of 0.4 mmcf/d.

### Drilling–Non-Operated

In 1996, Calahoo also participated in the drilling of three (0.3 net) horizontal oil wells at Nottingham, Saskatchewan. All the wells were successful and are producing 450 bbls/d (40 bbls/d net) of light oil. The net cost for the horizontal drilling program was $0.2 million. Calahoo also participated in four (1.0 net) non-operated wells (3 exploratory, 1 development) drilled by joint venture partners. Unfortunately, all four wells were unsuccessful. The net cost to Calahoo was less than $0.4 million.

### Workovers/Production Optimization

Calahoo operated or participated in a total of six recompletion operations. Three wells successfully tested gas and three wells were unsuccessful. Two of the non-operated wells in the Fort St. John area will be brought on-stream in the second quarter of 1997. One well in the Sedalia area, will be brought on-stream when facility capacity is available. The total net cost of Calahoo's 1996 production optimization activities was $0.3 million. The program resulted in net capped gas deliverability of 0.2 mmc/fd.

### Operations Summary

In 1996 Calahoo drilled or participated in a total of fourteen wells, completing four as oil wells, three as gas wells and seven dry and abandoned for a 52 percent success rate. On the recompletion side Calahoo was successful with three out of six prospects. Total 1996 capital allocated to drilling and recompletion was $3.6 million and resulted in production of 210 BOE/d, capped deliverability of 300 BOE/d and proved reserves of approximately 540 mBOE's.

## 1996 drilling activity

| | Year Ended December 31 | | |
|---|---|---|---|
| | 1996 | 1995 | 1994 |
| Oil (Gross/Net) | 4/1.2 | 6/1.4 | 4/1.8 |
| Natural Gas (Gross/Net) | 3/2.5 | 0/0 | 0/0 |
| Dry (Gross/Net) | 7/3.4 | 1/1 | 1/0.5 |
| Totals | 14/7.1 | 7/2.4 | 5/2.3 |

### 1997 Outlook

The outlook for 1997 is promising. Calahoo's capital budget for 1997 is estimated at $14 million (see Liquidity and Capital Resources), up 140 percent from the 1996 $5.8 million capital program. The priority for the year is to drill or participate in the drilling of at least 20 wells (14 net), a 170 percent net increase over last year's drilling program. In 1997, Calahoo plans to operate the drilling of 15 wells (11 net), split evenly between oil targets and gas targets. Half of these projects are being drilled on exploration plays generated in-house.

Calahoo will also continue to evaluate and pursue strategic property acquisitions during the year. As well, the Company intends to continue both its production optimization activities and purchases of land and seismic.

Calahoo's 1997 $14 million capital program is expected to add approximately 1,100 BOE/d net to our production base. The Company's 1997 exit production is forecast at approximately 2,000 BOE/d, with production for the year expected to average 1,450 BOE/d. Assuming oil prices based on $20 US/bbl WTI and a yearly average gas price of $1.35/mcf, 1997 cash flow is forecasted to average 20 cents per share, with exit annualized 1997 cash flow estimated at 27 cents per share.

### Conclusion

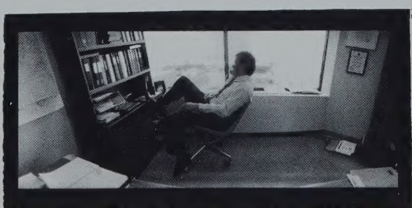
The performance of Calahoo common stock on the Alberta Stock Exchange in 1996 was greatly improved. Calahoo shares have appreciated from approximately 40 cents early in 1996 to a current price of 90 cents. Our share performance has likely been affected by an increased interest from larger financial institutions and brokerage houses and renewed "small cap" interest from the market in general. Calahoo will continue its efforts in enhancing and maintaining shareholder and financial institution relations.

1997 is a very important year for our Company. With a $14 million capital program planned, we have an excellent opportunity to add significantly to our reserve and production base. Our core area production has recently reached 1,000 BOE/d, and we expect continued improvements in these areas. We intend to aggressively pursue our development, exploration and acquisition activities in 1997 and carry a great deal of momentum into 1998.

At this time, I would like to express my gratitude to the Board of Directors and Calahoo's management, employees, consultants and contractors who have been instrumental in Calahoo's success to date. I would also like to thank our shareholders for their past, present and future support.

Sincerely yours,
Calahoo Petroleum Ltd.

Michael B. O'Hara. President and Chief Executive Officer
March 15, 1996



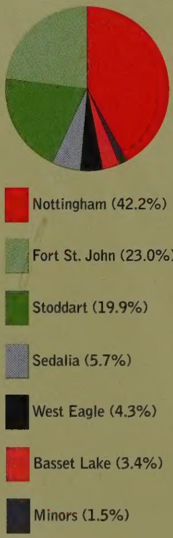
## OPERATIONS REVIEW

### current production by property*

| | Oil bbls/d | Gas mcf/d | NGLs bbls/d | Total BOE/d |
|---|---|---|---|---|
| Fort St. John/West Eagle | 177 | 960 | 9 | 282 |
| Stoddart | 107 | 1170 | 16 | 240 |
| Nottingham | 286 | 0 | 0 | 286 |
| Sedalia | 0 | 950 | 0 | 95 |
| Bassett Lake | 0 | 360 | 0 | 36 |
| Minor Properties | 8 | 0 | 0 | 8 |
| TOTALS | 578 | 3440 | 25 | 947 |

* Based on fourth quarter average production.

### cash flow distribution by property




### annual production by property

Average Daily Oil & NGL Production Volumes (bbls/d)

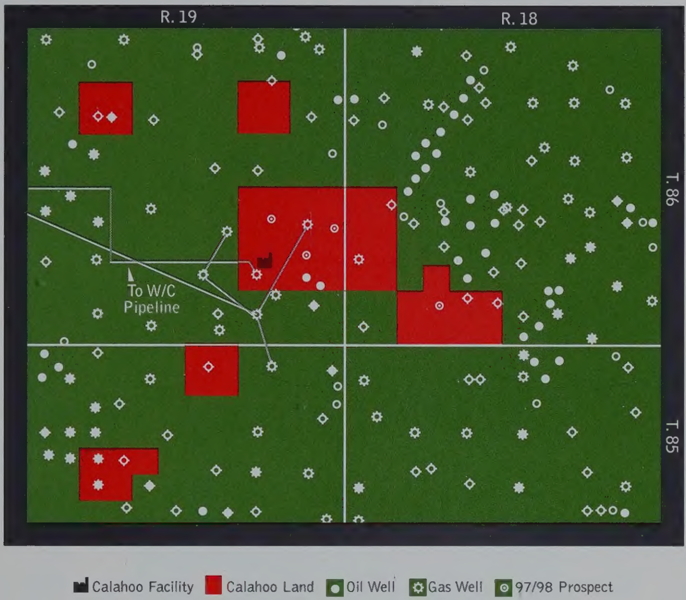
| Year Ended December 31 | 1996 | 1995 |
|---|---|---|
| Fort St. John/West Eagle | 187 | 156 |
| Stoddart | 78 | 16 |
| Nottingham | 277 | 276 |
| Minor Properties | 9 | 23 |
| Total Annual | 551 | 471 |

Average Daily Natural Gas Production Volumes (mcf/d)

| Year Ended December 31 | 1996 | 1995 |
|---|---|---|
| Fort St. John/West Eagle | 959 | 525 |
| Sedalia | 705 | 735 |
| Stoddart | 1,114 | 917 |
| Basset Lake | 375 | 321 |
| Total Annual | 3,153 | 2,498 |

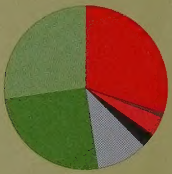
## MAJOR PROPERTIES

## Stoddart, B.C.



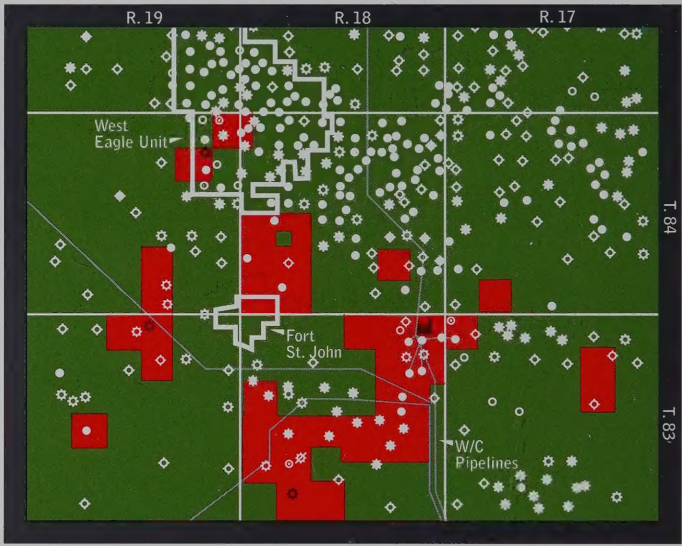

The Stoddart area is located two townships to the north of Fort St. John. Calahoo's production at Stoddart averaged 190 BOE/d in 1996, up 75% over 1995 production. Calahoo successfully drilled a 90% interest Stoddart development oil well in the third quarter of 1996 and a follow-up well is scheduled to be drilled immediately after spring break-up this year. Pending success, further drilling will proceed on the lands. Management closed an acquisition in February, 1997 that gives the Company a 67% interest in a second Stoddart gas well adding over 0.8 bcf net of sweet, rich gas reserves, and approximately 0.5 mmcf/d net of production. Included in the purchase is 2 sections (1.3 net) of prospective undeveloped land. Management also has recently negotiated and agreed on the terms for another acquisition from a partner, which will increase Calahoo's working interest by 10% in a gas well and in two oil wells. Calahoo also owns 6 sections of net undeveloped land in the area. The Company plans to drill at least 2 exploratory wells (1.2 net) at Stoddart in 1997. The wells, if successful, will lead to an aggressive development drilling program at Stoddart.

## production distribution by property



- Nottingham (30.1%)
- Fort St. John (27.1%)
- Stoddart (25.4%)
- Sedalia (10.0%)
- Basset Lake (3.9%)
- West Eagle (2.7%)
- Minors (0.8%)

# Fort St. John, B.C.




Calahoo Facility | Calahoo Land | Oil Well | Gas Well | 97/98 Prospect | Tie-in

Calahoo's largest operated property is located in the Fort St. John area of British Columbia. Light oil and solution gas is produced from six operated wells in the Airport North Pine oil pool. Five wells are 100 percent working interest and one well is 43.3 percent. All wells are pipeline connected to Calahoo's central battery and a solution gas compression/dehydration facility. Net average production in 1996 was 250 BOE/d (65 percent oil, 35 percent gas) up 35% over 1995 production. A 100 percent interest step out development well was drilled in January 1996. The primary oil zone came in low (wet), but the well was cased for a prospective gas zone uphole. Completion operations were unsuccessful and the well is being considered for area water disposal. Calahoo plans to drill one or two high interest wells on the property in 1997 and is continuing its efforts to purchase the remaining partner interests and/or prospective offsetting lands.

Over the last two years, Calahoo has substantially increased its capped gas reserves in the Fort St. John area through acquisitions and recompletions. At Taylor, immediately south of Fort St. John, Calahoo owns a 56% working interest in a capped Belloy gas well. The well was flow tested early this year and is capable of producing 1.2 mmcf/d gross. At West Fort St. John, Calahoo has a 30% interest in a Halfway gas well that flow tested at 0.7 mmcf/d gross. To the north, in the West Eagle area, a 100% well tested Baldonnel gas at 1.1 mmcf/d and management is negotiating with a third party for an equitable processing and compression arrangement. In 1996, a joint venture partner tied in a Cecil gas well (50 percent interest) which subsequently watered out in the summer. Management is currently evaluating the merit of performing a cement squeeze on the well or recompleting another wellbore in the same pool for Cecil gas production. Calahoo has budgeted for the above mentioned equipping and tie-in projects and intends to have the wells on-stream by year end at a combined net rate of 1.0 - 1.5 mmcf/d.

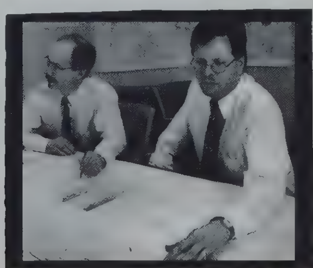
## Sedalia/Oyen, Alberta


Calahoo Facility   Calahoo Land   Oil Well   Gas Well   97/98 Prospect

Calahoo owns and operates two gas properties in the Sedalia/Oyen area of eastern Alberta. The area has excellent "low to medium risk" gas potential and over the next two years will provide Calahoo with opportunities to make cost-effective gains in gas reserves and production. Calahoo operates and owns 100% of the Sedalia and Oyen compression facilities and expects operating costs to average 35¢ per mcf. Typical capital costs to drill, complete and equip an 850 metre gas test well in this area is relatively inexpensive at $0.3 million.

A successful development well was drilled and tied in to Calahoo's compression facility in September. Two other development wells (1.5 net) were subsequently drilled in December and were successfully completed, and recently tied in. Current net production at Sedalia/Oyen is 1.4 mmcf/d from seven high-interest wells, up 100% from 1996 average production.

Calahoo plans to drill another 2 development wells (1.5 net) in the Sedalia/Oyen area in 1997. Contingent on seismic results, one high interest exploration well may also be drilled. Successful wells will be tied in and on-stream by year end. Calahoo owns over 6 net sections of undeveloped land in the Sedalia/Oyen area.



## Nottingham, Saskatchewan


Facility  Calahoo Land  Oil Well  Gas Well  97/98 Prospect

Calahoo holds an 8.5 percent interest in the Nottingham North Alida Beds Unit located in southeastern Saskatchewan. In 1996, Calahoo participated in two horizontal wells and one horizontal redrill, all of which were successful. Average stabilized production for the new wells is approximately 450 bbls/d (40 bbls/d net) of 42° API crude. Overall, the property averaged 280 bbls/d net to Calahoo in 1996. The operator has budgeted for the drilling of up to four more horizontal wells, scheduled to commence in the third quarter of 1997. The horizontal wells in this pool have typically paid out in less than 12 months. The Unit has excellent netbacks and a long reserve life. The Nottingham property has "paid out" for Calahoo and is expected to generate $1.4 million of operating income in 1997.

### Exploratory/Development Prospects

In a February and March land sale this year, Calahoo and a joint-venture partner successfully purchased over 6 sections of prospective land in the Rigel/Peejay area of British Columbia. As a result, Calahoo has three development Halfway oil locations to drill and one to two exploratory locations. The Halfway geological horizon, as evidenced by offsetting wells, holds excellent potential for prolific light oil production and long life reserves.

Calahoo drilled a 50% interest exploratory well in January, 1997 on a seismic anomaly at Dickins Lake in the northwest corner of the province. The well targeted gas in the Slave Point formation, and encountered over 150 m of reef, but unfortunately, the zone was tight and uneconomic. Calahoo earned a 27.5% working interest in several sections of land from a major company by drilling the well. The Company now owns a common 27.5% interest in over 22 sections of land in this area. Pending the outcome of further seismic activity, Calahoo anticipates drilling another well in the 1999 winter drilling season.

Calahoo has budgeted over $2 million of capital to pursue acquisitions, development and exploration projects in Alberta in an attempt to establish new core area(s) there. To date, Calahoo has identified some excellent acquisition and farm-in prospects including: Nisku oil in the Wood River and Fenn Big Valley area; Cardium oil in the Cynthia-Pembina area; and Keg River oil in the Rainbow area. Pending rig availability, Calahoo will drill the highly economic prospects in 1997.

### Land

Calahoo's quality and quantity of land, has been upgraded in 1996. The total net cost of Calahoo's land sale and seismic activity in 1996 was $0.9 million. In the Fort St. John/Stoddart area of British Columbia, Calahoo owns over 13 sections of undeveloped land and has over 8 sections of undeveloped land in other prospective areas in B.C. such as Buick Creek, West Stoddart, Rigel and Peejay. Five wells (2.9 net) are scheduled for drilling in 1997 on lands outside of the core areas . Calahoo also holds over 6 sections of undeveloped land in the Sedalia/Oyen area of Alberta.

## land holdings

| | Undeveloped | | Developed | | Total | |
|---|---|---|---|---|---|---|
| (acres) | Gross | Net | Gross | Net | Gross | Net |
| 1996 | 123,309 | 39,124 | 38,503 | 14,208 | 161,812 | 53,332 |

### Reserves

Calahoo's properties were evaluated by McDaniel and Associates as of January 1, 1997.

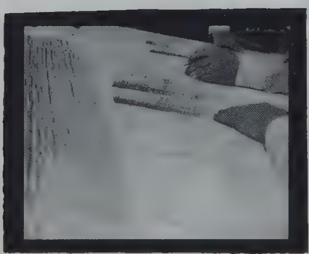
## reserves reconciliation

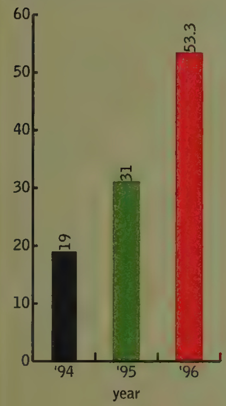
| | Oil & NGL's (mbbls) | | | Natural Gas (mmcf) | | |
|---|---|---|---|---|---|---|
| | Proven | Probable | Total | Proven | Probable | Total |
| January 1, 1996 | 950 | 613 | 1,563 | 11,095 | 4,365 | 15,460 |
| Production | (201) | — | (201) | (1,150) | — | (1,150) |
| Additions | 293 | — | 293 | 5,218 | 1,754 | 6,972 |
| Dispositions | (1) | (19) | (20) | (323) | (609) | (932) |
| January 1, 1997 | 1,041 | 594 | 1,635 | 14,840 | 5,510 | 20,350 |

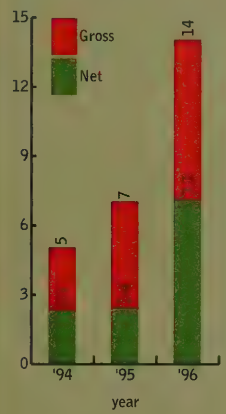
## reserve life index

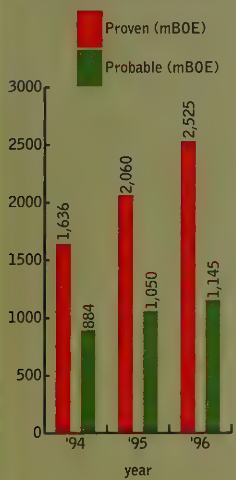
(Years of reserves left at 1996 annual average production rate)

| | 1996 Proven | Proven & Probable |
|---|---|---|
| Oil and NGLs | 5.2 | 8.1 |
| Natural Gas | 12.9 | 17.7 |
| BOE | 8.0 | 11.6 |

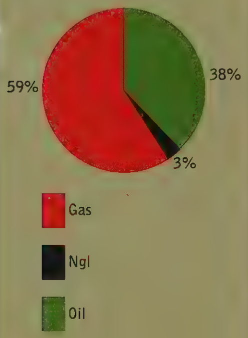




reserve distribution by product—total proved reserves




## present value of reserves

| | Reserves | | Discounted Value of Future Net Production Income $000s | | | |
|---|---|---|---|---|---|---|
| | Oil and NGL's (mbbls) | Natural Gas (mmcf) | $ 0% | $ 10% | $ 15% | $ 20% |
| Proven Producing | 1,010 | 9,591 | 32,990 | 21,097 | 17,982 | 15,742 |
| Proven Non-Producing | 31 | 5,249 | 5,745 | 2,774 | 2,117 | 1,680 |
| Probable (i) | 297 | 2,755 | 12,301 | 4,546 | 3,245 | 2,467 |
| ARTC | | | 453 | 306 | 265 | 235 |
| Total, January 1, 1997 | 1,338 | 17,595 | 51,489 | 28,723 | 23,609 | 20,124 |
| Total, January 1, 1996 | 1,257 | 13,280 | 43,211 | 23,301 | 18,910 | 15,926 |

(i) probable reserves reduced by 50% to allow for risk

## pricing forecast*

| | Crude Oil, WTI $US/bbl | Edmonton Light $Cdn/bbl | Natural Gas $Cdn/mcf |
|---|---|---|---|
| 1997 | 21.00 | 27.50 | 1.75 |
| 1998 | 20.00 | 26.10 | 1.95 |
| 1999 | 20.80 | 27.10 | 2.15 |
| 2000 | 21.60 | 28.20 | 2.30 |
| 2001 | 22.50 | 29.40 | 2.40 |
| 2015 | 41.60 | 54.80 | 4.85 |
| 2016 and thereafter | 43.50 | 57.30 | 5.20 |

* prepared by McDaniel & Associates

## reserve replacement

| | Proved | | Proved & Probable | |
|---|---|---|---|---|
| (BOE) | 1996 | 1995 | 1996 | 1995 |
| Total Proved Reserves Replaced | 815 | 734 | 990 | 898 |
| Annual Production | 316 | 263 | 316 | 263 |
| Reserves Replaced as a Percentage of Reserves Produced | 258% | 279% | 313% | 341% |

## annual finding and development costs

| Year ended December 31 | 1996 | 1995 | 1994 |
|---|---|---|---|
| Total capitalized costs ($000's) | 5,760 | 5,506 | 5,614 |
| Proven reserve additions (mBOE) | 815 | 734 | 700 |
| Average cost per BOE | $7.07 | $7.50 | $8.02 |
| Proven and probable reserve additions (mBOE) | 990 | 898 | 1,469 |
| Average cost per BOE | $5.82 | $6.13 | $3.82 |

## recycle ratio *

| 1996 | 1995 |
|---|---|
| 1.7 | 1.3 |

* based on proved & risked probable

## cumulative finding and development costs

| | 1994 - 1996 |
|---|---|
| Total capitalized costs ($000's) | 16,880 |
| Proven reserve additions (mBOE) | 2,249 |
| Average cost per BOE | $7.51 |
| Proven and probable reserves additions (mBOE) | 3,357 |
| Average cost per BOE | $5.03 |

Calahoo's net asset value (less long term debt) is 80 cents per share. The net asset calculation is based on the January 1, 1997 McDaniels and Associates' evaluation of total proved and risked probable reserves.

## net asset value

| | 10% DCF ($ million) | 15% DCF ($ million) |
|---|---|---|
| Total Proved | 24.2 | 20.4 |
| * Probables (Risked at 50 percent) | 2.3 | 3.2 |
| Total Proved and Probable | 26.5 | 23.6 |
| Undeveloped Land/Seismic | 2.5 | 2.5 |
| Current Debt and working capital (Dec/96) | (4.9) | (4.9) |
| | 24.1 | 21.2 |
| Net Asset Value / Share | $0.90 | $0.80 |

The calculation, represents a 25 percent increase over the net asset value calculated last year.

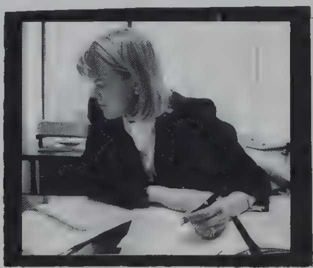
## total capital expenditures

($ millions)

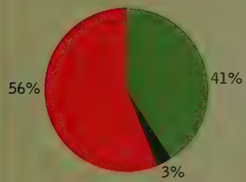
| | 1996 | 1995 |
|---|---|---|
| Land | 0.5 | 0.5 |
| Seismic | 0.4 | 0.2 |
| Drilling and Completion | 2.9 | 1.0 |
| Equipment and Facilities | 0.7 | 0.7 |
| Acquisitions and Other | 1.3 | 2.7 |
| TOTAL | 5.8 | 5.1 |

## Marketing Arrangements

In 1996 Calahoo sold its oil at Nottingham and Fort St. John/Stoddart to Volant Energy and Husky Oil Operations Ltd. respectively and to Petro Source Canada beginning in 1997. The average oil price received at the wellhead was $28.26. Ninety-five percent of Calahoo's oil production is light, averaging 38° API. The majority of our natural gas has been contracted through CanWest Gas Supply Inc. in B.C. and TransCanada Gas Services Inc. in Alberta, giving us stability in our natural gas revenue.

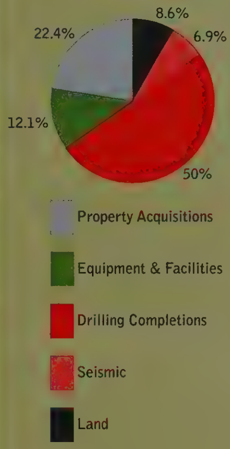


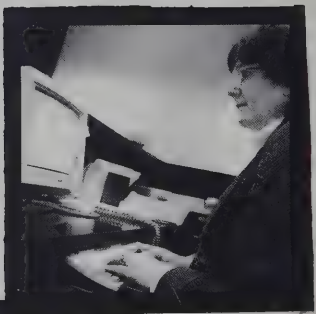
## reserve distribution by product—proved & probable reserves

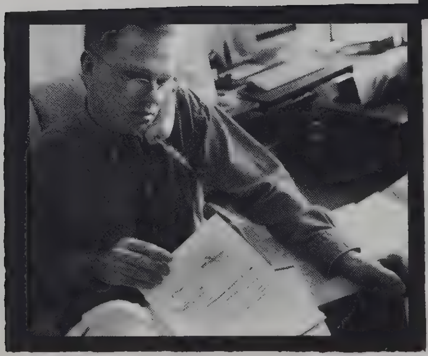



## capital expenditures

(as a percentage of 1996 total of $5.8 million)







MANAGEMENT'S DISCUSSION AND ANALYSIS

## Overview

Major financial highlights for 1996 include a 54 percent increase in cash flow from operations and a 43 percent increase in gross revenues over 1995. These gains were primarily due to a 20 percent increase in average daily production coupled with a strong increase in both crude oil and natural gas prices.

## Revenues

oil and natural gas revenues

| ($000's) | 1996 | 1995 | % CHANGE |
|---|---|---|---|
| Oil and Liquids | 5,326 | 3,895 | 37 |
| Natural Gas | 1,628 | 974 | 67 |
| Other | 47 | 37 | 27 |
| Gross Revenue | 7,001 | 4,906 | 43 |
| Net Royalties | (1,413) | (935) | 51 |
| Net Revenue | 5,588 | 3,971 | 41 |

The Company continues to focus on three core properties: Fort St.John/Stoddart in Northeastern British Columbia, Nottingham in Southeastern Saskatchewan and Oyen/Sedalia in Southeastern Alberta. The production from these core properties accounts for 95 percent of total corporate revenues.

Oil and gas sales increased 43 percent in 1996 to $7 million from $4.9 million in 1995. Production increased 20 percent to 866 barrels daily of oil equivalent in 1996 compared to an average of 721 barrels daily of oil equivalent in 1995. 1996 exit production was approximately 1,000 barrels daily of oil equivalent, compared to 882 in 1995. The production increases resulted from successful drilling in the Stoddart, Sedalia/Oyen and Nottingham areas.

netbacks

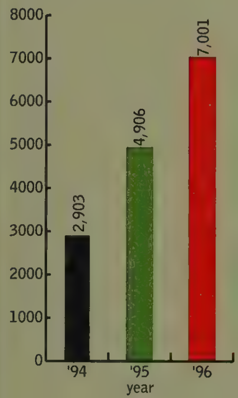
| | Oil and Gas Liquids ($/bbl) 1996 | Natural Gas ($/mcf) 1996 | Total ($/BOE) 1996 | Total ($/BOE) 1995 |
|---|---|---|---|---|
| Revenue | $27.93 | $1.37 | $23.05 | $18.65 |
| Royalties, net of ARTC | (5.48) | (0.21) | (4.45) | (3.56) |
| Production Expenses | (2.27) | (0.43) | (3.13) | (3.02) |
| Hedging gain (loss) | (1.53) | — | (0.97) | — |
| Netback | $18.65 | $0.73 | $14.50 | $12.07 |

In 1996, oil and natural gas liquid revenues increased to $5.3 million from $3.9 million in 1995. This increase was the combined result of both higher oil prices and increases in production. The average oil price received in 1996 was $28.26 per barrel, an increase of 23 percent from the 1995 average of $22.92. Production increased 17% to 551 barrels per day in 1996 from 471 barrels per day in 1995.

Natural gas revenue increased by 67 percent in 1996 to $1.6 million from $0.9 million in 1995. This increase was due to a 26 percent production increase and higher natural gas prices. The average gas price received in 1996 was $1.37 per thousand cubic feet compared to $1.04 for 1995. These averages are calculated using wellhead prices received in British Columbia for approximately 65% of the Company's gas production.

The Company realized a hedging loss of approximately $0.3 million after entering into a fixed price contract at $19.08 U.S. from May to December 1996.

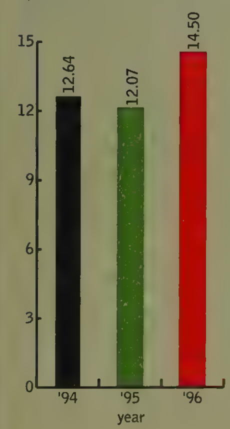
gross revenue
(thousands of dollars)




### Royalties

Calahoo's average royalty rate, before Alberta Royalty Tax Credit (ARTC), averaged 20 percent in 1996, similar to 1995. Production from Saskatchewan is affected by the 75 Mstb royalty holiday for horizontal wells, resulting in royalty rates of 29 percent at Nottingham. Royalty rates for other core properties were in the 14 percent range. In 1996 the Company received ARTC of approximately $26,000. Calahoo also received $47,000 in royalty payments from other operators through its overriding interests in certain producing lands.

operating netbacks
($/BOE)




### Operating Expenses

operating expenses

| | 1996 | 1995 | 1994 |
|---|---|---|---|
| Operating Expenses ($000's) | 994 | 794 | 456 |
| Average Cost ($/BOE) | 3.13 | 3.02 | 3.06 |

Calahoo's operating expenses increased to $1 million in 1996 from $0.8 million in 1995. This increase is a direct result of increases in production for the same period. Operating expenses, on a per barrel of oil equivalent basis, increased marginally in 1996 to $3.13 from $3.02 in 1995.

### General and Administrative

general and administrative expense

| ($ thousands) | 1996 | Per BOE | 1995 | Per BOE |
|---|---|---|---|---|
| Gross Expenses | 1,199 | $3.78 | 752 | $2.86 |
| Overhead Recoveries | (144) | (0.45) | (108) | (0.41) |
| G & A | 1,055 | 3.33 | 644 | 2.45 |
| Capitalized G & A | (430) | (1.36) | (241) | (0.92) |
| Reported G&A Expense | 625 | $1.97 | 403 | $1.53 |

General and administrative expenses for 1996 were $0.6 million ($1.97/BOE), compared with $0.4 million ($1.53/BOE) in 1995. G&A expenses of $0.4 million were capitalized, compared to $0.2 million in 1995. Higher G&A expenses were largely the result of the increase in Calahoo's staffing levels required to complete the team to manage the Company's growing asset base. It is expected that reported net G&A will be approximately $1.58/BOE for 1997.

### Interest Expense

interest expense

| $000's | 1996 | 1995 | % Change |
|---|---|---|---|
| Interest Expense | 420 | 481 | (13) |
| Average Cost ($/BOE) | 1.33 | 1.83 | (27) |
| Debt Outstanding at Year End | 4,070 | 6,828 | (40) |
| Cash Flow Times Interest Coverage | 8 | 5 | 60 |
| Debt to Fourth Quarter Annualized Cashflow Ratio | 1.0:1 | 2.7:1 | (63) |

Interest expense for 1996 was $0.4 million compared to $0.5 million in 1995. This decrease reflects lower costs of borrowing in 1996, resulting from both a decrease in the prime lending rate and a decrease in the Company's borrowing rate per a revised term loan agreement. Average debt outstanding was consistent with 1995.

### Depletion and Depreciation

depletion and depreciation

| | 1996 | 1995 | % CHANGE |
|---|---|---|---|
| Depletion & Depreciation expense ($000's) | 2,162 | 1,397 | 55 |
| Rate per BOE (10 mcf:1 bbl) | $6.82 | $5.31 | 28 |

The depletion, depreciation and site restoration provision for 1996 was $2.2 million compared to $1.5 million in 1995, largely due to an increased asset base combined with a 2 percent higher depletion rate on a unit of production basis. The depletion and depreciation rate, based on the Company's full cost accounting policy of converting gas to oil equivalent on a 10 mcf:1 bbl basis, averaged $6.82 per boe during 1996 compared to $5.31 in 1995.

### Income and Capital Taxes

income and capital taxes

| | 1996 | 1995 | % CHANGE |
|---|---|---|---|
| Capital Taxes ($000's) | 152 | 80 | 90 |
| Deferred Income Taxes ($000's) | 500 | 193 | 159 |
| Effective Deferred Tax Rate (%) | 38 | 23 | 65 |

Capital taxes for 1996 were $152,000 compared to $80,000 for 1995. The increase is due to additional Saskatchewan Capital Tax and Large Corporation tax as a result of increased revenue from Saskatchewan and the increased capital base of the Company. Deferred income taxes increased to $0.5 million from $0.2 million in 1995. Deferred income tax was first recorded in 1995, as this was the first year the Company's tax pools did not exceed the book pools. As at December 31, 1996, Calahoo had approximately $16 million of available tax pools and with planned capital programs for 1997 and beyond, Calahoo should not be taxable for the next few years.

### Cash Flow and Net Earnings

Cash flow increased by 54 percent to $3.4 million in 1996 from $2.2 million in 1995. Weighted average cash flow per share increased by 23 percent and reached $0.16 in 1996 compared with $0.13 in 1995. Fully diluted cash flow per share decreased by 1 percent to $0.10 in 1996 from $0.11 in 1995 due to a public issue of share capital in late December of 1996.

Net earnings grew 15 percent in 1996 to $0.7 million from $0.6 million in 1995. Weighted average net income per share remained consistent with 1995 at $0.03 in 1996.

items affecting cash flow and net earnings

| | 1997 Forecast $/BOE | 1996 $/BOE | 1995 $/BOE |
|---|---|---|---|
| Oil and Natural Gas Revenue | 20.77 | 22.08 | 18.65 |
| Net Royalties | (3.95) | (4.45) | (3.56) |
| Operating Expenses | (3.00) | (3.13) | (3.02) |
| Net Operating Income | 13.82 | 14.50 | 12.07 |
| General and Administrative | (2.03) | (1.97) | (1.53) |
| Interest | (0.67) | (1.33) | (1.83) |
| Capital Taxes | (0.19) | (0.48) | (0.30) |
| Cash Flow from Operations | 10.93 | 10.72 | 8.41 |
| Depletion and Depreciation | (6.61) | (7.08) | (5.31) |
| Deferred Taxes | (2.08) | (1.58) | (0.95) |
| Net Income | 2.24 | 2.06 | 2.15 |

### Liquidity and Capital Resources

In 1996, Calahoo strengthened its balance sheet by raising equity by way of both a private placement (raising $1.6 million in June, 1996) and a public flow-through share financing which raised $2.7 million in December, 1996. These funds were used to finance the Company's $5.8 million capital expenditure program and reduce debt. At December 31, 1996, the Company had $4.1 million of bank debt on a revolving term credit facility of $8.0 million.

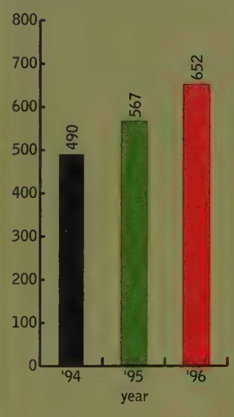
The Company has budgeted approximately $14 million for capital expenditures in 1997 (subject to regular review) which will be financed by cash flow, bank debt and equity. Bank debt is expected to remain at one and a half times cash flow in 1997. Equity funding will come from the exercise of warrants. Currently, the Company has 6.05 million share purchase warrants outstanding which, upon exercise, have the potential of bringing $4.6 million into share capital in 1997.

### Business Risks

The oil and gas industry is subject to risks not only in the finding and developing of petroleum and natural gas reserves, but also with respect to commodity prices, interest rates and environmental concerns. Calahoo attempts to mitigate these risks by:

- Focusing on activities and areas in which it has proven expertise;
- Developing and exploring prospects in close proximity to the Company's core areas;
- Owning and operating production and processing facilities wherever possible to control amount and timing of capital expenditures;
- Maintaining a Corporate Environmental Policy and Programme that is communicated to all field operations by management.

net earnings
(thousands of dollars)



The results of operations are sensitive to changes in commodity prices, foreign exchange rates and interest rates. The following table summarizes those sensitivities:

### sensitivities—1997 estimates

| Change In: | Cash Flow $000's | Per Share |
|---|---|---|
| Oil Price ($1.00 Cdn/bbl) | 300 | 1¢ |
| Gas Price ($0.10 Cdn/mcf) | 200 | 0.5¢ |
| Oil Volume (100 bbls per day) | 410 | 1.5¢ |
| Gas Volume (1,000 mcf per day) | 270 | 1¢ |
| Exchange rate ($0.01 in US/Cdn exchange rate) | 58 | — |
| Canadian Prime Rate (1%) | 60 | — |

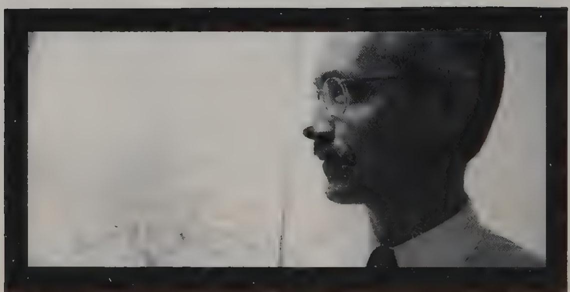
Calahoo is exposed to interest expense fluctuations since the bank facility is at a variable rate. To minimize interest rates, Calahoo borrows through bankers' acceptances. Calahoo's 1996 interest obligation was well covered by both earnings and cash flow during the year.

Calahoo, from time to time, also employs commodity price hedging on a portion of its production to mitigate extraordinary price swings. For 1997 the Company has entered a fixed pricing agreement for 250 bbls of oil per day at $23 US WTI for second quarter production. Management will continue to review our hedging position and will engage in further hedging at suitable prices.

**Outlook**

Over the past year, Calahoo concentrated its efforts in developing a substantial inventory of oil and gas prospects for future exploration and development. The Company now has sufficient stable cash flow to enable it to take on an aggressive drilling program and a few higher risk and reward opportunities.

The 1997 capital expenditure budget totals approximately $14 million which is the largest for Calahoo to date. Approximately 20 wells will be drilled, with the Company expecting to add over 1,000 BOE/d of production by December 1997. Overall, we expect to average 1,450 BOE/d for 1997, split between 800 bbls/d of oil and 6,500 mcf/d of natural gas. Based on average selling prices of $20.00 US WTI per bbl for oil and $1.35 per mcf for gas, Calahoo forecasts that cash flow from operations will be $5.8 million ($0.20 per share) for 1997.



## MANAGEMENT'S REPORT TO THE SHAREHOLDERS OF CALAHOO PETROLEUM LTD.

The accompanying financial statements and all other information presented in this annual report are the responsibility of the Company's management.

The financial statements have been prepared by management in accordance with accounting principles generally accepted in Canada. The Company's internal controls have been designed and maintained by management to provide reasonable assurance that assets are properly safeguarded and that the financial records are sufficiently well maintained to provide relevant, timely and reliable information to management and to allow preparation of the financial statements in accordance with the Company's accounting policies. Where necessary, certain estimates are made by management. The financial statements have been prepared within reasonable limits of materiality and within the framework of the significant accounting policies as summarized in the notes to the financial statements.

Deloitte & Touche, an independent firm of chartered accountants, have been appointed by the Shareholders to examine the financial statements and to report to the Shareholders. The Audit Committee, consisting of directors, a majority of whom are not employees of the Company, have reviewed the financial statements, including the notes thereto, with management and Deloitte & Touche. The financial statements have been approved by the Board of Directors on the recommendation of the Audit Committee.

Michael B. O'Hara
President and Chief Executive Officer

Jill T. Angevine
Controller

## AUDITORS' REPORT TO THE SHAREHOLDERS OF CALAHOO PETROLEUM LTD.

We have audited the balance sheets of Calahoo Petroleum Ltd. as at December 31, 1996 and 1995 and the statements of earnings and retained earnings and of changes in financial position for the years ended December 31, 1996 and 1995. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with generally accepted auditing standards. Those standards require that we plan and perform an audit to obtain reasonable assurance whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation.

In our opinion, these financial statements present fairly, in all material respects, the financial position of the Company as at December 31, 1996 and 1995 and the results of its operations and the changes in its financial position for the years ended December 31, 1996 and 1995, in accordance with generally accepted accounting principles.

Deloitte & Touche

Calgary, Alberta
March 7, 1996

Chartered Accountants

## STATEMENTS OF EARNINGS AND RETAINED EARNINGS

Calahoo Petroleum Ltd.

| For The Years Ended December 31 | 1996<br>$ | 1995<br>$ |
|---|---|---|
| **Revenue** | | |
| Oil and gas | 7,000,916 | 4,906,016 |
| Royalties | (1,446,840) | (959,866) |
| Alberta royalty tax credit | 33,604 | 24,423 |
| | 5,587,680 | 3,970,573 |
| **Expenses** | | |
| Oil and gas production | 993,855 | 793,989 |
| General and administrative | 625,451 | 403,316 |
| Interest on long-term debt | 420,467 | 481,259 |
| Depletion and depreciation | 2,244,024 | 1,452,177 |
| | 4,283,797 | 3,130,741 |
| **Earnings before income taxes** | 1,303,883 | 839,832 |
| Deferred tax provision (Note 6) | 500,000 | 193,000 |
| Large corporations and capital taxes | 151,951 | 80,086 |
| **Net earnings** (Note 7) | 651,932 | 566,746 |
| **Retained earnings, beginning of year** | 1,057,520 | 490,774 |
| **Retained earnings, end of year** | 1,709,452 | 1,057,520 |

## BALANCE SHEETS

Calahoo Petroleum Ltd.

| As At December 31 | 1996 $ | 1995 $ |
|---|---|---|
| **Assets** | | |
| **Current** | | |
| Accounts receivable | 1,765,698 | 1,024,388 |
| Petroleum and natural gas properties (Note 3) | 18,471,391 | 14,873,536 |
| | 20,237,089 | 15,897,924 |
| **Liabilities** | | |
| **Current** | | |
| Accounts payable | 2,689,066 | 963,954 |
| Long-term debt (Note 4) | 4,070,766 | 6,827,908 |
| Future site restoration costs | 168,961 | 86,961 |
| Deferred income taxes (Note 6) | 1,047,369 | 249,000 |
| | 7,976,162 | 8,127,823 |
| **Shareholders' Equity** | | |
| Share capital (Note 5) | 10,551,475 | 6,712,581 |
| Retained earnings | 1,709,452 | 1,057,520 |
| | 12,260,927 | 7,770,101 |
| | 20,237,089 | 15,897,924 |

APPROVED BY THE BOARD

Director

Director

## STATEMENTS OF CHANGES IN FINANCIAL POSITION

| Calahoo Petroleum Ltd.<br>For The Years Ended December 31 | 1996<br>$ | 1995<br>$ |
|---|---|---|
| **Net inflow (outflow) of cash related to the following activities:** | | |
| **Operating** | | |
| Net earnings | 651,932 | 566,746 |
| Items not affecting cash | | |
| Depletion and depreciation | 2,244,024 | 1,452,177 |
| Deferred income taxes | 500,000 | 193,000 |
| Funds provided by operations | 3,395,956 | 2,211,923 |
| Changes in non-cash operating working capital items | 621,541 | (136,740) |
| Cash provided by operating activities | 4,017,497 | 2,075,183 |
| **Financing** | | |
| (Decrease) increase in long-term debt | (2,757,142) | 2,585,100 |
| Issue of share capital on acquisition of subsidiary (Note 2) | — | 414,246 |
| Issue of share capital, net (Note 5) | 4,137,263 | 544,023 |
| Cash available for investing | 5,397,618 | 5,618,552 |
| **Investing** | | |
| Acquisition of petroleum and natural gas properties | (1,289,988) | (2,662,368) |
| Drilling, facilities, land and seismic expenditures | (4,469,892) | (2,430,304) |
| Acquisition of subsidiary company (Note 2) | — | (414,246) |
| Changes in non-cash investing working capital items | 362,262 | (110,595) |
| Other | — | (1,039) |
| Cash invested | 5,397,618 | (5,618,552) |

## NOTES TO THE FINANCIAL STATEMENTS

### 1. SIGNIFICANT ACCOUNTING POLICIES

The financial statements have been prepared in accordance with generally accepted accounting principles, and reflect the following policies:

#### Petroleum and Natural Gas Properties

The Company follows the full cost method of accounting in accordance with the guideline issued by the Canadian Institute of Chartered Accountants whereby all costs associated with the exploration for and development of petroleum and natural gas reserves, whether productive or unproductive, are capitalized in a Canadian cost centre and charged to income as set out below. Such costs include lease acquisition, drilling, geological, and overhead expenses related to exploration and development activities. Costs of acquiring and evaluating unproved properties are excluded from depletion calculations until it is determined whether or not proved reserves are attributable to the properties or impairment occurs.

Gains or losses are not recognized upon disposition of petroleum and natural gas properties unless crediting the proceeds against accumulated costs would significantly alter the rate of depletion.

Depletion is provided on accumulated costs using the unit of production method. For purposes of the depletion calculation, estimated proven petroleum and natural gas reserves are converted to a common unit of measure on the basis of their approximate relative energy content.

The net carrying value of the Company's petroleum and natural gas is limited to an ultimate recoverable amount. This amount is the aggregate of future net revenues from estimated proved reserves and the costs of unproved properties, net of impairment allowances, less future general and administrative costs, financing costs, restoration and abandonment costs, and income taxes. Future net revenues are estimated using year end prices and all costs are assumed to be constant.

#### Office Equipment

Depreciation of office equipment is provided by a straight-line method at a rate of 20% per annum.

#### Flow-through Shares

During both 1996 and 1995, the Company issued flow-through shares to finance a portion of its capital expenditure program. Pursuant to the terms of the flow-through share agreements, the tax deductions associated with the expenditures have been renounced to the subscribers. Accordingly, share capital has been reduced and deferred income taxes recorded equal to the estimated amount of future income taxes payable by the Company as a result of the renunciations.

#### Joint Venture Accounting

A portion of the Company's exploration and production activities is conducted jointly with others and, accordingly, these financial statements reflect only the Company's proportionate interest in such activities.

#### Financial Instruments

Financial instruments are used to manage exposures related to commodity prices. They are not used for speculative trading purposes. Gains and losses on commodity price hedges are included in revenues on the sale of the related production.

#### Future Site Restoration

The estimated cost of site restoration is based on the current cost of the anticipated method and extent of site restoration in accordance with existing legislation and industry practice. The annual provision is provided for on a unit of production basis and is included in depletion and depreciation.

## 2. ACQUISITIONS

On April 1, 1995, the Company acquired all of the outstanding shares of Planet Oil and Gas Ltd. ("Planet") for a purchase price of $414,246. Planet was 40% owned by three directors of the Company. The purchase price was satisfied by issuance to Planet shareholders of 726,748 Class A voting common shares of the Company.

The acquisition has been accounted for by the purchase method. The results of operations of Planet have been included in these financial statements from the date of acquisition. Effective January 1, 1996, Planet was amalgamated with the Company.

Details of the assets and liabilities acquired are as follows:

| | $ |
|---|---|
| Working capital | 75,276 |
| Property and equipment | 1,031,765 |
| Long-term debt | (692,795) |
| | 414,246 |

## 3. PETROLEUM AND NATURAL GAS PROPERTIES

| | Cost $ | Accumulated Depletion and Depreciation $ | December 31 1996 Net Book Value $ | Cost $ | Accumulated Depletion and Depreciation $ | December 31, 1995 Net Book Value $ |
|---|---|---|---|---|---|---|
| Properties and equipment | 22,989,107 | 4,591,150 | 18,397,957 | 17,280,157 | 2,456,150 | 14,824,007 |
| Office equipment | 134,323 | 60,889 | 73,434 | 83,394 | 33,865 | 49,529 |
| | 23,123,430 | 4,652,039 | 18,471,391 | 17,363,551 | 2,490,015 | 14,873,536 |

For the year ended December 31, 1996, the Company capitalized $195,000 (1995 - $130,000) of overhead costs related to exploration and development.

The cost of acquiring and evaluating unproved properties excluded from the depletion base as at December 31, 1996 was $1,591,892 (1995 - $1,493,316).

## 4. LONG-TERM DEBT

The bank loan is a revolving term loan that bears interest at a rate of prime plus 1/2 of 1% (prime plus 5/8% at December 31, 1995) per annum. Fixed and floating charge debentures on the properties of the Company and a general assignment of book debts have been granted as security.

The maximum amount of borrowing currently available under this revolving bank loan facility is $8,000,000 (1995 - $7,000,000). In accordance with the loan agreement as at February 24, 1997, the Company has $4,500,000 in bankers' acceptances as part of its outstanding debt, at an interest rate of 4.6% expiring on May 26, 1997. The undrawn portion at December 31, 1996 is $3,929,234.

The fair value of debt at year end is equal to its carrying value due to the floating interest rate nature and revolving nature of the facility. The Company is exposed to interest expense fluctuations since the loan facility is at a variable rate.

The cash balance is zero at the end of the period as a result of a daily positioning arrangement whereby funds on deposit are netted against the loan balances at the Company's bank.

## 5. SHARE CAPITAL

Authorized

Unlimited number of Class A voting common shares

Unlimited number of Class B non-voting common shares

Unlimited number of Class C non-cumulative, non-voting, redeemable preferred shares

| Common shares issued | Number of Shares | Amount $ |
|---|---|---|
| Balance, December 31, 1994 | 16,996,434 | 5,810,312 |
| Shares issued for the acquisition of Planet | 726,748 | 414,246 |
| Issued for cash: | | |
| Private placement of flow-through shares | 1,218,110 | 548,150 |
| Tax benefits renounced | — | (56,000) |
| Share issuance costs | — | (4,127) |
| Balance, December 31, 1995 | 18,941,292 | 6,712,581 |
| Issued for cash: | | |
| Private placement of common shares | 3,813,800 | 1,758,346 |
| Stock options | 27,500 | 13,750 |
| Public offering of flow-through shares | 3,800,000 | 2,660,000 |
| Shares issued for employee stock purchase plan | 93,721 | 28,116 |
| Share issuance costs | — | (322,949) |
| Tax benefit of share issue costs | — | 185,771 |
| Tax benefits renounced | — | (484,140) |
| Balance, December 31, 1996 | 26,676,313 | 10,551,475 |

### Options

At December 31, 1996, the Company had 2,292,500 (1995 - 1,453,800) employee and director stock options outstanding exercisable at $0.39 to $0.74 per share which expire at varying dates to 2001.

### Flow-through Common Shares

During 1995, the Company issued 1,218,110 common shares for $548,150. The terms of these shares provide that the Company renounce tax deductions in the amount of $548,150 all of which were renounced by December 31, 1996.

### Warrants

During 1996, the Company issued 3,000,000 units at $0.54. Each unit consists of one common share and 3/4 of warrant. At December 31, 1996, 2,250,000 warrants are outstanding at an exercise price of $0.65 until June 30, 1997, or $0.75 until June 30, 1998.

By way of a prospectus dated December 10, 1996, the Company issued 3,800,000 units at $0.70. Each unit consists of one flow-through common share and one warrant. As at December 31, 1996, 3,800,000 warrants are outstanding at an exercise price of $0.82 until June 15, 1997. The terms of the 3,800,000 common shares provide that the Company renounce tax deductions in the amount of $2,660,000 of which $668,116 were incurred and renounced to December 31, 1996.

## 6. INCOME TAXES

The provision for income taxes differs from the amounts that would have resulted had the combined federal and provincial statutory tax rate been applied to the earnings for the year as follows:

| Years Ended December 31, | 1996 $ | 1995 $ |
|---|---|---|
| Computed income tax expense at statutory tax rate of 45.45% | 592,615 | 367,466 |
| Increase (decrease) resulting from: | | |
| Non-deductible crown charges | 529,353 | 330,209 |
| Resource allowance | (563,614) | (384,375) |
| Alberta Royalty Tax Credit | (15,273) | (10,830) |
| Other | (43,081) | (1,830) |
| | 500,000 | 300,640 |
| Utilization of income tax deductions not previously recognized for accounting purposes | — | (107,640) |
| Provision for income taxes | 500,000 | 193,000 |

At December 31, 1996, the Company had income tax pools available to reduce future years' income for tax purposes of approximately:

| | $ |
|---|---|
| Canadian oil and gas property expense | 7,922,826 |
| Canadian development expense | 2,032,855 |
| Canadian exploration expense | 3,018,788 |
| Undepreciated capital costs | 2,705,966 |
| Earned depletion | 344,000 |
| | 16,024,435 |

## 7. EARNINGS AND FUNDS FLOW PER SHARE

| Years Ended December 31, | 1996 $ | 1995 $ |
|---|---|---|
| Earnings per share | | |
| - basic | 0.03 | 0.03 |
| - fully diluted | 0.03 | 0.03 |
| Funds flow per share | | |
| - basic | 0.16 | 0.13 |
| - fully diluted | 0.16 | 0.13 |
| Weighted average number of common shares | 20,994,170 | 17,692,171 |

## 8. HEDGING ACTIVITIES

Effective May 1, 1996, the Company entered into a fixed price contract to hedge against general reductions in oil prices. The agreement called for the Company to sell 250 barrels of oil per

day, at $19.08 U.S., until December 31, 1996.

The Company has entered into a fixed price contract for 250 barrels per day for the second quarter of 1997 at $23.00 U.S.

## four year summary

| Financials ($000'S, except per share amounts) | Year Ended December 31 1996 | 1995 | 1994 | Six Months ended December 31 1993 |
|---|---|---|---|---|
| Gross Revenue | 7,001 | 4,906 | 2,903 | 562 |
| Cash Flow from Operations | 3,396 | 2,212 | 1,461 | 260 |
| Basic and fully diluted per share | $0.16 | $0.13 | $0.10 | $0.03 |
| Net Earnings | 652 | 567 | 490 | 112 |
| Basic and fully diluted per share | $0.03 | $0.03 | $0.03 | $0.01 |
| Capital Expenditures | 5,760 | 5,093 | 5,614 | 3,770 |
| Long-Term Debt | 4,071 | 6,828 | 3,550 | 2,306 |
| Shareholders' Equity | 12,261 | 7,770 | 6,301 | 3,352 |
| Common Shares Outstanding (000's) | | | | |
| Basic | 26,676 | 18,941 | 16,996 | 12,846 |
| Fully Diluted | 35,018 | 20,395 | 18,370 | 13,690 |
| Weighted Average | 20,994 | 17,692 | 14,313 | 8,461 |
| **Operations** | | | | |
| Average Daily Production | | | | |
| Oil and NGLs (bbls/d) | 551 | 471 | 317 | 140 |
| Natural Gas (mcf/d) | 3,153 | 2,498 | 915 | 230 |
| Total (BOE/d) | 866 | 721 | 409 | 163 |
| Average Sales Price | | | | |
| Oil and NGLs ($/bbl) | 27.93 | 22.67 | 20.67 | 20.09 |
| Natural Gas ($/mcf) | 1.37 | 1.04 | 1.57 | 1.40 |
| Operating Costs ($/BOE) | 3.13 | 3.02 | 3.06 | 3.35 |
| Operating Netbacks ($/BOE) | 14.50 | 12.07 | 12.64 | 12.48 |
| General and Administrative Costs ($/BOE | 1.97 | 1.53 | 1.51 | 2.75 |
| **Reserves** | | | | |
| Oil and NGLs (mbbls) | | | | |
| Proven | 1,041 | 950 | 1,000 | 734 |
| Probable | 594 | 614 | 688 | 22 |
| Total | 1,635 | 1,564 | 1,688 | 756 |
| Natural Gas (mmcf) | | | | |
| Proven | 14,840 | 11,095 | 6,360 | 3,888 |
| Probable | 5,509 | 4,370 | 1,960 | 13 |
| Total | 20,349 | 15,465 | 8,320 | 3,901 |
| **Wells Drilled** [Gross (net) ] | | | | |
| Oil | 4(1.2) | 6(1.4) | 4(1.8) | 7(0.5) |
| Natural Gas | 3(2.5) | 0(0) | 0(0) | 0(0) |
| Dry | 7(3.4) | 1(1.0) | 1(0.5) | 0(0) |
| Totals | 14(7.1) | 7(2.4) | 5(2.3) | 7(0.5) |
| **Land Holdings** (Acres) | | | | |
| Gross | 161,812 | | | |
| Net | 53,332 | 31,000 | 19,000 | 1,800 |
| Average Interest | 33.0% | | | |

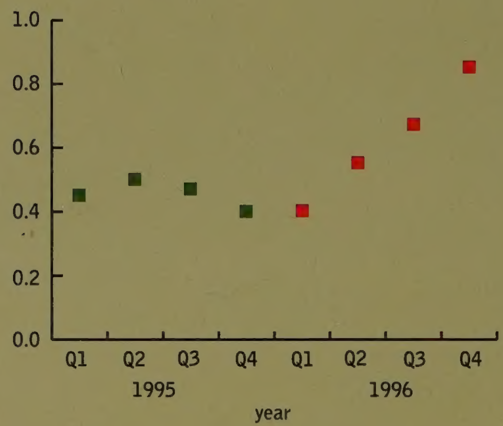
## quarterly financial summary

| Financial | 1996 Q1 | 1996 Q2 | 1996 Q3 | 1996 Q4 | 1995 Q1 | 1995 Q2 | 1995 Q3 | 1995 Q4 |
|---|---|---|---|---|---|---|---|---|
| (000's, except per share amounts) | | | | | | | | |
| Gross Revenues | 1,598 | 1,564 | 1,628 | 2,211 | 1,051 | 1,256 | 1,186 | 1,413 |
| Cash Flow from Operations | 819 | 737 | 846 | 994 | 535 | 570 | 476 | 631 |
| Basic and fully diluted | $0.04 | $0.03 | $0.04 | $0.05 | $0.03 | $0.03 | $0.03 | $0.04 |
| Net Earnings | 204 | 131 | 172 | 145 | 294 | 182 | (157) | 316 |
| Basic and fully diluted | $0.01 | $0.01 | $0.01 | $0.01 | $0.02 | $0.01 | ($0.01) | $0.01 |
| **Operating** | | | | | | | | |
| Oil and NGLs (bbls/d) | 553 | 513 | 532 | 603 | 433 | 442 | 471 | 548 |
| Natural Gas (mcf/d) | 3,202 | 2,739 | 3,118 | 3,447 | 1,218 | 2,538 | 2,896 | 3,297 |
| Oil and NGLs ($/bbl) | 23.99 | 27.36 | 28.11 | 30.86 | 23.30 | 24.66 | 21.60 | 21.70 |
| Natural Gas ($/mcf) | 1.15 | 1.09 | 1.25 | 1.99 | 1.08 | 1.06 | 0.97 | 1.05 |

| Common Share Trading Information | 1996 Q1 | 1996 Q2 | 1996 Q3 | 1996 Q4 | 1995 Q1 | 1995 Q2 | 1995 Q3 | 1995 Q4 |
|---|---|---|---|---|---|---|---|---|
| High ($/share) | $0.50 | $0.55 | $0.72 | $1.10 | $0.52 | $0.60 | $0.54 | $0.50 |
| Low ($/share) | $0.35 | $0.40 | $0.47 | $0.69 | $0.40 | $0.40 | $0.44 | $0.38 |
| Close ($/share) | $0.40 | $0.55 | $0.69 | $0.85 | $0.45 | $0.50 | $0.47 | $0.40 |
| Volume (thousands) | 801 | 1,403 | 1,208 | 10,121 | 421 | 436 | 234 | 380 |
| Trading Value ($000's) | $327 | $647 | $690 | $9,384 | $194 | $212 | $112 | $162 |

### closing share price

($/share)



## directors

Michael B. O'Hara, P.Eng.
President & Chief Executive Officer

Mark J. Powell, P.Geol.
Vice President - Exploration

Jihad A. Shibley, P.Eng.
Vice President - Engineering

Robert V. Heathcott, P.Land
President of Heather Oil Ltd.

Michael J. Lang, B.Sc. MBA
Treasurer and Chief Financial Officer
Beau Canada Exploration Ltd.

E. Mitchell Shier, LL B, LL M
Ballem MacInnes
Barrister and Solicitors

## officers and key personnel

Michael B. O'Hara
President & Chief Executive Officer

Mark J. Powell
Vice President - Exploration

Jihad A. Shibley
Vice President - Engineering

E. Mitchell Shier
Secretary

Jill T. Angevine
Controller

## bankers

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Main Branch
Calgary, Alberta

## solicitors

Ballem MacInnes
Calgary, Alberta

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## stock listing

The Alberta Stock Exchange
Symbol CLX

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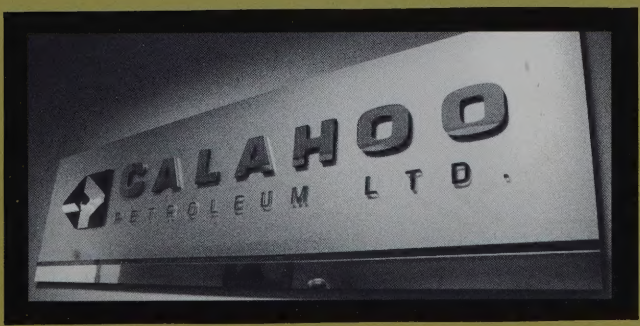
## abbreviations

| | |
|---|---|
| bbls | barrels |
| bbls/d | barrels per day |
| bcf | billion cubic feet |
| BOE | barrels of oil equivalent (gas @ 10 mcf:1) |
| BOE/d | barrels of oil equivalent per day |
| mcf | thousand cubic feet |
| mcf/d | thousand cubic feet per day |
| mBOE | thousands of barrels of oil equivalent |
| mmcf | million cubic feet |
| mmcf/d | million cubic feet per day |
| NGLs | natural gas liquids |



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